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SUBJECT: SECURITIZATION LAW TO GENERATE NEW LIQUIDITY IN MARKET

Summary

¶1. El Salvador's new Securitization Law will allow the conversion of private projects in liquid securities to be traded in the stock market. The Law is expected to energize the capital market and open the financing options for private and public sector projects such as toll roads and new housing developments. It will be especially beneficial for diversifying the pension funds. The complexity of the law and the general concept of securitization, however, may impede its widespread use. End summary.

Background

¶2. The Legislative Assembly approved on November 15, 2007, a Securitization Law. The Central Bank had been working in the Securitization Law since 2001, modeled after Chile's successful law, and the law had been under consideration in the National Assembly since 2005. Ultimately, the law passed with support from ARENA, the PDC, and the PCN. The FMLN opposed the law, and the CD abstained.

¶3. The law permits the conversion of project assets into Securitization Funds (Fondos de Titularizacion in Spanish). The funds are generated from the alienation of cash flow-generating assets. The law requires securitization issuers to be constituted as anonymous fixed capital entities of indeterminate term domiciled in El Salvador. The fund will be an independent asset. Project capital may not be less than \$1 million and the assets securitized must generate periodic and predictable cash flows.

¶4. The Superintendent of the Stock Market is responsible for implementation and compliance and will charge issuers 0.75 percent of total annual revenues. In order to speed implementation of the law, Salvadoran Stock Exchange authorities are holding meetings with the Superintendent of the Stock Market to plan and conduct training and public education. The Stock Market will also bring in a Bolivian expert to conduct training and discuss issues Bolivia faced during implementation.

Public Sector Beneficiaries

¶5. In the near term, the securitization law is expected to aid in the growth and diversification of the pension funds. Currently, the pension funds have limited investment options. Under the Pension Law, the funds are allowed to invest up to 20 percent in Salvadoran-issued public securities.

¶ 6. According to stock market officials, the Government of El Salvador is also considering financing public works projects through securitization, including possible toll roads. The Lempa River Executive Hydroelectric Commission (CEL) is also considering securitizing new electricity generation projects.

Private Sector View

¶ 7. Accordingly to Stock Exchange Legal Representative Julio Vega, several players are waiting to take advantage of the law. For example, "CrediQ Inversiones I" a financial subsidiary of "Grupo Q," a Salvadoran automotive company with a presence in Central America and Panama, offers auto loans. Securitizing those loans could free up new capital for further expansion in the region. The Salvadoran Construction Chamber (CASALCO), non-bank mortgage broker "La Hipotecaria," the Housing Social Fund (Fondo Social para la Vivienda), and the Popular Housing National Fund (FONAVIPO) have all expressed interest in securitizing their projects and loans. Though with recent crisis in the U.S. sub-prime mortgage market has made headlines here and development of those projects could be impacted. Stock Exchange officials also expect credit card issuers to securitize their debt issuances and maquila companies to securitize their export contracts to obtain more financing in order to expand their investment.

Comment

¶ 8. The securitization law is a long-awaited positive development for the financial markets and the first of three outstanding financial reforms - securitization, investment funds, and regulatory body reform -- to pass the assembly. The Investment Fund law is expected to pass before March. While the securitization law should

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increase liquidity and help fund new capital projects, Stock Exchange authorities acknowledge two major impediments. First, securitization is a completely new financial concept in El Salvador, and many firms are unclear on how it might be used. Second, the law itself is so complicated that firms may be slow to adopt it.

Glazer